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WORKING PAPER

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FAR EAST/PACIFIC BRANCH

INTELLIGENCE HIGHLIGHTS NO. 59
13 JULY - 19 JULY 1949

SECTION I. SUMMARY OF FAR EAST TRENDS AND DEVELOPMENTS

Most Far Eastern nations have remained noncommittal in response to the Chiang-Quirino proposal for an anti-Communist "Pacific Union" (p. 2).

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The Republic of Korea has asked that UN military observers be posted along the "incident"-ridden 38th Parallel (p. 3).

The Chinese Communists have announced the beginning of a new "major offensive" in central China after a two-month lull in operations (p. 4). Meanwhile, Communist intransigence in the treatment of foreigners appears to be threatening future relations with the West to the Communists' own possible disadvantage (p. 6).

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The marginal notations used in succeeding sections of this Weekly ("A", "B", or "C") indicate the importance of the items in R/FE opinion with "A" representing the most important.

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SECTION II. DEVELOPMENTS IN SPECIFIED AREAS

GENERAL

Reactions to "Pacific Union" Proposal--The Chiang-Quirino proposal for a "Pacific Union", to counteract and contain Asiatic Communism, has been received with little enthusiasm. Both the apparent unwillingness of the US to support such a bloc and the fact that initiative for the envisioned union came from the "retired" leader of the prostrate and discredited Chinese Nationalist Government evidently have caused most Asiatic nations to hesitate before indicating their attitudes. "A"

Three areas -- Nationalist China, the Philippines, and the Republic of Korea -- have endorsed the plan. Other countries, however, have been either noncommittal or entirely silent. The Prime Minister of Thailand has deferred a decision in the matter by saying that Thailand has not been invited to participate in the union. The Burmese Foreign Minister stated on 14 July that Burma "may favorably consider" the formation of a Pacific bloc if it would work for world peace and prosperity. However, he questioned the effectiveness of such a union in combatting the Communist threat in Southeast Asia.

According to Philippine President Quirino, representatives of the Indonesian Republic now in the Philippines are enthusiastic. The Netherlands Minister to the Philippines, however, has been instructed not to commit himself. In Indochina, the diplomatic counselor to the French High Commissioner is worried over the implications of Vietnamese cooperation with the Chinese Nationalists, fearing that such action would be interpreted as interference in Chinese internal affairs and constitute an invitation for a Communist attack on Indochina. Australia and New Zealand have made no comment.

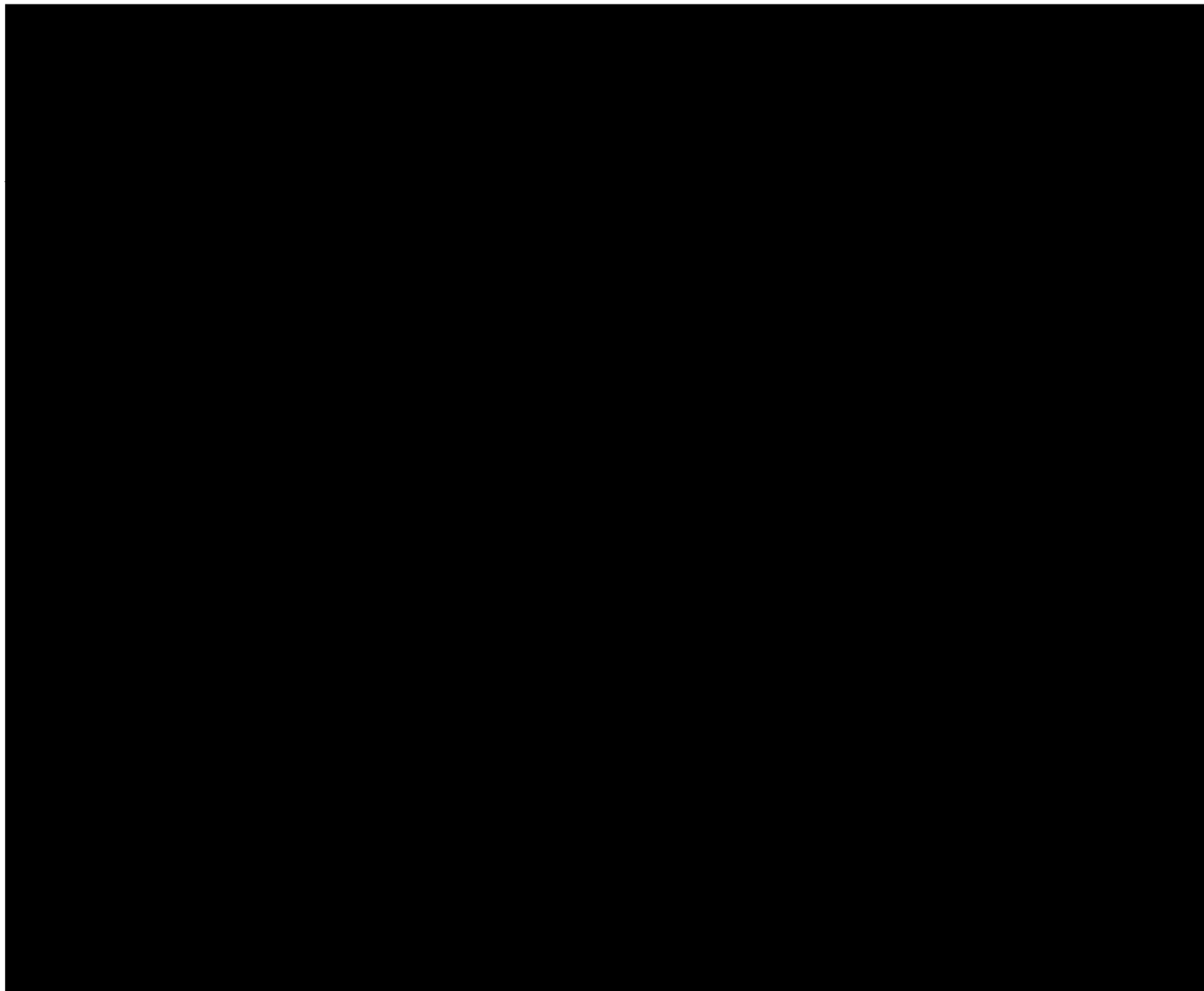
Invitations to a preliminary conference to discuss the formation of the union have not yet been issued. Before doing so, President Quirino plans to recall Ambassador Romulo from his post at the UN, to interrogate Pacific nations as to their recommendations. Meanwhile, Quirino, Chiang, and Korea's President Rhee will undoubtedly continue to press for US support which, if received, would be a strong inducement for the participation of other presently noncommittal nations.

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KOREA

Republic requests UN Border Observers--In a recent letter, the Foreign "B"
Minister of the Republic of Korea suggested to the United Nations Com-
mission on Korea (UNCOK) that a unit of UN military observers be estab-
lished in Korea, to work with UNCOK in halting attacks by northern Korean
forces along the 38th parallel.

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A previous proposal for UN military observers had been considered by UNCOK during April and May, 1949, but the matter was dropped without action being taken. At that time, Commission members were divided on the possible effectiveness and advisability of observers in Korea. The UN Secretariat, further, informed UNCOK on that occasion that UN military observers were sent to the field as a result of Security Council or General Assembly action. The Secretariat stated that since the US was withdrawing its armed forces from Korea, it could be presumed that America, at least, was satisfied that no threat to international peace existed in the area and for this reason there appeared to be little justification for a military observers' mission.

The pressure of the present formal Korean request for observers may force UNCOK to re-open the question. On the basis of recent inspections of trouble spots along the parallel, the Commission, if it so chose, could adopt a resolution for presentation to the fall meeting of the UN General Assembly stating that a threat to international peace exists in Korea and recommending the dispatch of military observers. However, it is probable that, unless the US strongly supports the Korean suggestion for observers, UNCOK will avoid further action during the final weeks of the Commission's stay in Korea.

CHINA

New Communist Offensive starts--In central China, the two month lull in "A" military operations has apparently ended. Peiping radio announced that Communist armies had launched a "major offensive" along a front extending eastward from the Yangtze gorges in Hupeh to the middle reaches of the Kan River in Kiangsi. Peiping radio claimed several important victories, including the capture of Ichang and Shasi (west of Hankow) and Kian and Anfu (south of Nanchang). The Nationalist later claimed that Kian was retaken in a counter-attack. The Communist offensive, according to a Shanghai dispatch, is aimed in the direction of Canton, some 4-500 miles to the south. The only sizable Nationalist force between the Communists and Canton is the 175,000-strong Army commanded by PAI Chung-hsi. PAI is expected to withdraw into Kwangsi as soon as the Communists approach his present positions in the area about Changsha. Once fully under way, the Communist regulars, aided by irregulars already operating in south China and by the absence of firm Nationalist resistance, should be able to roll into Canton in about 30 days.

Arbitrary taxation of foreign firms--Communist authorities recently have imposed arbitrary levies on business concerns which discriminate particularly against foreign companies. Although nominally imposed as income

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taxes, the assessments bear no clear relation to earnings. The amounts charged apparently were determined arbitrarily on the basis of what the traffic could bear. Thus far, these taxes have been imposed in two cities. In Hankow, a levy totaling over US\$600,000 was imposed; in Tientsin, the levy totalled US\$2,000,000. It is expected that Shanghai will soon follow suit with a very much larger levy.

Most foreign firms do not have sufficient cash reserves to pay such taxes. As a result, they are faced with the alternative of drawing funds from abroad or else liquidating local stocks and capital equipment. Foreign businesses are apprehensive that these taxes will serve as precedents for further arbitrary assessments in the near future and that such taxes will be deliberately applied in some areas to squeeze out the foreign competition in favor of government trading organizations.

Agricultural disasters will delay recovery---Communist China is mobilizing "B" for an all-out fight against a series of agricultural disasters which have plagued the countryside during the past several months. Some million acres of rice land in the Yangtze valley have been flooded, spring drouths have damaged crops in north China and south Manchuria and locust swarms have further reduced northern yields. The Communist press is filled with directives regarding famine counter-measures and dyke-building.

This threat to the food supply will undoubtedly force the Communists to divert much of their energy from the task of rehabilitation to the job of salvaging crop production. Coarse grains with short growing seasons are being planted in the north with a chance of maturing before autumn frosts. Secondary dykes are being thrown up to keep the flood waters of the Yangtze from inundating new crop areas. The revenues of the Communist regime, nonetheless, will be cut seriously and general economic recovery in Communist China will be delayed by the reduced supply of food and raw materials for domestic consumption or export.

Ambitious five-year rail plan---The Communist All-China Railroad Regulatory Conference has okayed a five-year plan to restore China's existing 16,700 miles of rail line completely and to add another 6,600 miles of track to the system. Railroads have already been given a high priority on manpower and raw material allocations by the Communists, and they are working to rehabilitate the lines they now control. Communist successes in rehabilitation to date have been achieved through a process of cannibalization which has left the lines weak and inefficient. Double-tracked lines are now single-tracked ones; bridges, ties, rails and ballasting are often of an emergency nature. The Communists will soon arrive at a point where cannibalization is no longer rewarding and, with further expansion, will find

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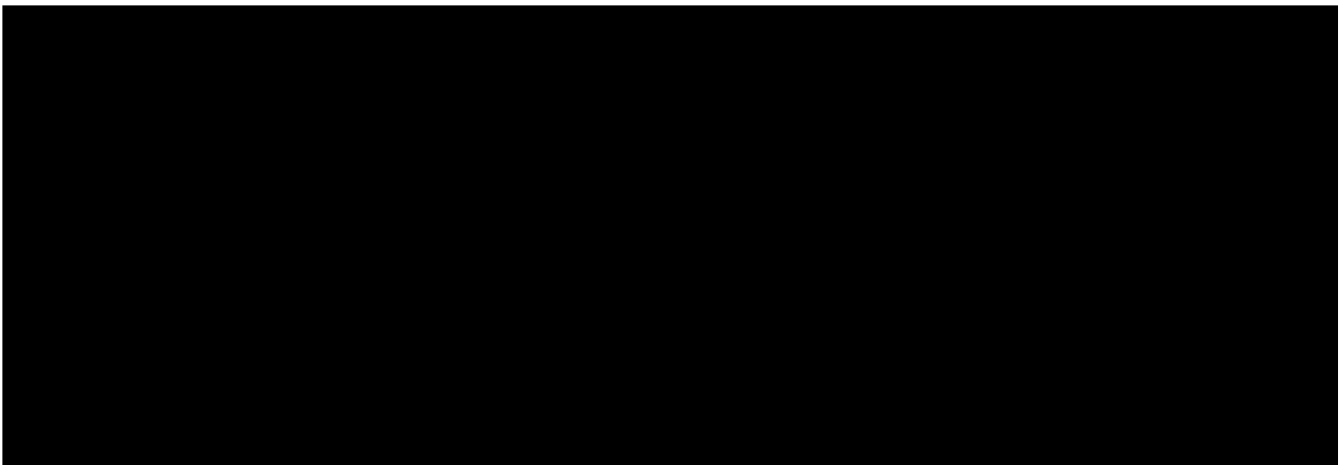
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themselves facing a shortage of rolling stock and locomotives. In all, restoration of China's rail system is estimated to require at least US\$300 million of imports. The CCP should consider the rebuilding of existing lines an amply ambitious project; expansion in the next five years seems a grandiose dream.

Persecution of Foreigners may backfire--Communist authorities in the Yangtze Valley are doing nothing to halt the abuse of foreigners, particularly Americans, in that area and the harsh treatment of foreigners apparently has either the direct sanction or the implied approval of local Communist officials. Nanking authorities have insisted on "shop guarantees" for Ambassador Stuart and his party before the issuance of exit permits for his return to the US. These regulations require that all claims against departing foreigners must either be satisfactorily settled, or assumed by a responsible person or firm remaining behind, before any travel permit will be issued. If the "shop guarantee" formula is universally applied, it could conceivably result in a situation whereby all foreigners remaining in China would find themselves hostages for those already departed. "B"

Anti-foreignism, as exemplified in a number of Shanghai incidents, may derive from a reaction to Communist propaganda, lately intensified by the strained economic position of the blockaded city. It further reflects Communist inexperience in city administration, and strong Communist suspicion of "imperialist" influences in general. The end result of continued anti-foreignism will be to deprive Communist China of the services of foreign money and skills and adversely affect Communist chances of recognition by Western Powers. Unless curbed, the nationalistic impulse so carefully nourished by the Communists may well prove disadvantageous to them.

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